

Tax Type: USE TAX  
Issue: Use Tax On Leased Items  
Temporary Storage (Exemption)

STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
SPRINGFIELD, ILLINOIS

THE DEPARTMENT OF REVENUE )  
OF THE STATE OF ILLINOIS )  
 )  
v. ) Docket #  
 )  
XXXXXX ) IBT #  
 )  
Taxpayer )

APPEARANCES XXXXX, for XXXXX (hereinafter the "Taxpayer").

A prehearing conference was conducted prior to hearing at which the parties agreed to certain stipulations, which were entered into this record by my 3/23/94 order. The Department and the Taxpayer stipulated as follows:

1. XXXXX (hereinafter "Taxpayer A") is located in XXXXX and does not have employees permanently stationed in Illinois.
2. Taxpayer B (hereinafter "Taxpayer B") is a corporation that does business both inside and outside of the State of

Illinois.

3. During the audit period there were true leases in effect between Taxpayer A as lessor and Taxpayer B as lessee.
4. The lease property that is at issue in this matter was delivered by Taxpayer A to Taxpayer B in Illinois where Taxpayer B first took possession of said property.

I point out that I as administrative law judge am not necessarily bound by stipulations where one covers an arguable conclusion of law, such as No. 3, regarding true leases. In this case, however, my review of documentary evidence submitted by both parties causes me to agree that the disputed transactions herein are actually leases, and are not conditional sales.

At the hearing, Ms. XXXXX, Point of Sale Supervisor for Taxpayer B, a lessee of Taxpayer, testified about Taxpayer B's business relationship with Taxpayer and referenced certain of Taxpayer's exhibits. Taxpayer Exhibit Nos. 1 through 9 were introduced into evidence and these included Taxpayer's master lease agreement, lease schedules and backup, and product purchase and escrow agreements.

The prima facie case of the Department was established by the admission of its Exhibit Nos. 1 through 3 into evidence and these included the corrected return (Dept. Ex. No. 1) and the audit workpapers. (Dept. Ex. No. 2). The contested issue in this matter is if certain property Taxpayer leases in Illinois is entitled to the temporary storage exemption if the lessee eventually moves the property to another state.

After considering this matter, I recommend the issue be resolved in favor of the Department.

FINDINGS OF FACT I find the facts to be as stipulated between the parties in Stipulations 1 through 4. In addition I find:

1. Taxpayer conducted business in Illinois during the audit period

by leasing and occasionally selling computers, cash registers and related equipment. (Dept. Ex. No. 2).

2. Taxpayer prepared its Illinois sales tax returns from the sales and lease information it maintained at its Center, XXXXX headquarters. (Dept. Ex. No. 2, p. 19).

3. The Department issued Notice of Tax Liability (NTL) No. XXXXX on June 22, 1993 for \$183,395.00 tax, \$18,340.00 penalty and \$71,182.00 interest, with Taxpayer given credit for a \$1,929.00 payment leaving a net liability due of \$270,988.00. (Dept. Ex. No. 3).

4. As a lessor, Taxpayer did cause lease assets to be transferred to its Lessee Taxpayer B. As a lessee, Taxpayer B maintained dominion and control over the lease assets at its various Illinois locations. (Dept. Ex. No. 2; Tr. p. 66).

5. Many of the leased registers, computers, etc. that Taxpayer B maintained in Illinois were kept at their XXXXX distribution center location for weeks or months and then sent to other stores outside of Illinois. (Taxpayer Ex. No. 2; Tr. p. 16).

6. Taxpayer's lessee kept many of the lease items at their XXXXX location for 3 through 14 months, or longer. (Tr. p. 70; Taxpayer Ex. No.3).

7. The entire liability herein is based upon assets Taxpayer leased to Taxpayer B under Lease Schedules D, E, F, G, H, I and J. (Dept. Ex. No. 2).

CONCLUSIONS OF LAW A Tax is imposed upon the privilege of using tangible personal property in Illinois.<sup>1</sup> The word "use" is defined in the Use Tax Act<sup>2</sup> as the exercise of ownership power over tangible personal property such as the cash registers, computers and related electronic equipment that Taxpayer rented in the instant case.

Illinois case law has clearly established that a lessor of tangible

personal property in Illinois incurs a Use Tax liability because it exercises incidents of ownership over the leased property, even though the leased item is in the physical possession of the lessee.<sup>3</sup> This principle is also enunciated in Department regulations.<sup>4</sup>

In the instant case there is no dispute that Taxpayer is a lessor and that the property it is leasing is held by its lessee in Illinois. Taxpayer is requesting application of the temporary storage exemption to some of this rental property. This exemption is set out in Section 3-55 of the Use Tax Act<sup>5</sup> where it states in pertinent part:

Multistate exemption. To prevent actual or likely multistate taxation, the tax imposed by this Act does not apply to the use of tangible personal property in this State under the following circumstances:

\* \* \*

- (e) The temporary storage, in this State, of tangible personal property that is acquired outside this State and that, after being brought into this State and stored here temporarily, is used solely outside this State or is physically attached to or incorporated into other tangible personal property that is used solely outside this State or is altered by converting, fabricating, manufacturing, printing, processing, or shaping, and, as altered, is used solely outside this State.

In this case, as in all tax exemption cases, a taxpayer's claim that items are tax exempt must be analyzed in the context that entitlement to exemption must be proven by the taxpayer, and doubts regarding the applicability of the exemption will be resolved in favor of taxation. A party claiming an exemption has the burden to prove clearly and demonstrate conclusively that he is entitled to the exemption. (Christian Action Ministry v. Department of Local Government Affairs 74 Ill. 2d 51, 62 (1978); Telco Leasing, Inc. v. Allphin 63 Ill. 2d 305, 310 (1976); LeTourneau Railroad Services, Inc. v. Department of Revenue 134 Ill. App. 3d 638, 642 (1985)). In this case Taxpayer has cited no authority that directly supports its claim for exemption. What Taxpayer has done is attempt to distinguish Telco Leasing and Philco Corp. and to argue by

analogy that two temporary storage cases support its position. I do not agree.

It is clear that Taxpayer is using its property in Illinois under the authority of Philco and Telco, and Taxpayer acknowledges this. (Taxpayer Brief p. 13). Because Taxpayer is using the property at issue here in Illinois as "use" is defined in the Use Tax Act, Taxpayer is precluded from the exemption because one of its requirements is that the property be "used solely outside this State." An item of rental property cannot be used solely outside Illinois when it has already been used in Illinois by the lessor in its business of leasing. The exemption is limited to situations where the use is "solely outside this State", *United Air Lines v. Mahin* 49 Ill. 2d 45, 55 (1971), and that is not the situation herein.

I therefore find that it was correct and proper for the auditor to assess Use Tax upon the items of tangible personal property Taxpayer was leasing to Taxpayer B in Illinois. Also, the "temporary" requirement of the exemption may not be met here for many of the items as several stayed in Illinois for months and some for periods in excess of a year. (Taxpayer Ex. No. 3).

Taxpayer also makes a fairness argument regarding the possibility of multistate taxation<sup>6</sup> on the basis it may have paid rental receipts taxes in other states after removal of the leased property from Illinois. This argument is really not applicable here because the credit allowed in Section 3-55 (d) for another State's tax is only available when a person "... has already paid a tax in another State..." and in the instant case Taxpayer has not paid a tax in another State before using the property in Illinois in its rental business.

Taxpayer also asks for a reduction of the NTL on the basis its Ex. No. 1 Annex C shows it paid Illinois Use Tax. While Taxpayer did pay some tax, my review of Annex C in conjunction with the audit file shows that the

payments represented by check Nos. XXXXX (6/19/90), XXXXX (2/18/92), and XXXXX (7/31/90) were accounted for and credited by the auditor in his audit work. (Dept. Ex. No. 2, pp. 32, 37, 67, 69, 75-76).

The remaining checks do contain some payments for items in issue here, but not the entire amount of each check. Check No. XXXXX for \$9,399.00 (7/20/92) only contained an amount of \$1,232.00 tax attributable to Taxpayer B lease schedule G, the remainder being for property not in issue here that went to XXXXX. Similarly, check No. XXXXX for \$15,272.00 (7/20/93) only contains \$2,760.00 on Taxpayer B lease H items, the remainder being for XXXXX items. Check No. XXXXX for \$3,510.00 (12/18/92) only contains \$1,758.00 for Taxpayer B lease I items and check No. XXXXX for \$13,247.00 (10/20/93) only contains \$1,256.26 for Taxpayer B lease J items. Based upon this examination, I recommend Taxpayer be given credit for a total of \$7,006.00 tax paid on the various Taxpayer B lease items.

In summary, except for the \$7,006.00 tax paid to the Department, I find the Taxpayer has not overcome the prima facie case of the Department.

RECOMMENDATION Based upon my aforementioned findings of fact and conclusions of law, I recommend the Department reduce NTL No. XXXXX and issue a final assessment.

Karl W. Betz  
Administrative Law Judge

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1. 35 ILCS 105/3.
  2. 35 ILCS 105/2 and 3.
  3. Philco Corp v. Dept. of Revenue 40 Ill. 2d 312 (1968). Telco Leasing, Inc. v. Allphin 63 Ill. 2d 305 (1976).
  4. 86 Admin. Code ch. I, Secs. 130.2010 and 150.305 (e).
  5. 35 ILCS 105/3-55
  6. 35 ILCS 105/3-55(d)